No. 87-1054

Supreme Court, U.S.
FILED
JUN 9 1988
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

THE FIRESTONE TIRE & RUBBER CO., *et al.*,
Petitioners,

v.

RICHARD BRUCH, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES AND THE NATIONAL ASSOCIATION OF MANUFACTURERS AS *AMICI CURIAE* IN SUPPORT OF THE PETITIONERS

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June 9, 1988

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTION PRESENTED

Amici curiae will address the following question:

Whether the court of appeals erred in refusing to apply an arbitrary and capricious standard of review under ERISA to a plan administrator's benefits determination solely because the administrator, like most plan administrators covered by ERISA, was employed by the company that had established the plan.

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BRIEF *AMICI CURIAE* IN SUPPORT OF THE PETITIONERS

INTEREST OF THE *AMICI CURIAE*

With the written consent of the parties,[1] the Chamber of Commerce of the United States ("Chamber") and the National Association of Manufacturers of the United States of America ("NAM") submit this brief as *amici curiae* in support of petitioners. The Chamber is the nation's largest federation of businesses, representing more than 180,000 corporations, partnerships and proprietorships, as well as several thousand trade and professional associations and state and local chambers of commerce. The NAM is a voluntary business association of over 13,000 companies, employing 85 percent of all manufacturing workers and producing over 80 percent of the nation's manufactured goods. The NAM also is affiliated with 158,000 additional businesses through its Associations Council and the National Industrial Council. Both the Chamber and the NAM regularly advocate their members' views in court on issues of national concern to the business community, and, in fact, *amici* previously submitted a brief in this case urging the Court to grant certiorari.

In the decision below, the Third Circuit held that the traditional "arbitrary and capricious" standard of judicial review does not apply to all denials of claims for employee benefits that are covered by the Employee Retirement Income Security Act of 1974 (ERISA). According to the Third Circuit, that standard is inappropriate when (a) a trustee whose salary is paid by the employer (b) administers a benefit plan under which benefits are paid from the general assets of the employer. The court of appeals held that the trustee in such circumstances faces a potential conflict of interest and therefore the trustee's decisions should be subject to *de novo* judicial

[1] Pursuant to Rule 36 of the Rules of this Court, the parties have consented to the filing of this brief. The parties' letters of consent have been filed with the Clerk of this Court.

review, even when there is no showing that the trustee faces an actual conflict of interest.

Both the Chamber's and the NAM's memberships include many companies which maintain their own pension and welfare benefit plans, many of which are administered by employees of the companies and funded from the employers' general assets. The Third Circuit's decision not only would lead to a drain of funds available for employee benefits by requiring continuous *de novo* litigation of claim denials, but also would overload the federal judiciary and contravene the enforcement scheme Congress established in ERISA. Accordingly, *amici* wish to present their views in order to provide this Court with a legal framework that better balances the employees' legitimate concern that claim denials be based on the requirements of the plan with Congress' intent that the regulatory structure of ERISA not discourage employers from establishing benefit plans.

STATEMENT

The Employee Retirement Income Security Act

In passing the Employee Retirement Income Security Act of 1974 (ERISA), Congress responded to widespread and growing public demands for pension plan reform by enacting minimum standards for pension plan administration. 119 Cong. Rec. S16867 (daily ed. September 19, 1973) (statement of Senator Hartke); 29 U.S.C. § 1001. Under ERISA, workers can rely upon the promise of a future pension and look forward to "a retirement with financial security and dignity and without fear that [they] will be lacking in the necessities to sustain them as human beings within our society." H.R. Rep. No. 533, 93d Cong., 1st Sess. 8 (1973). Congress also enacted safeguards for employee welfare plans, *i.e.*, employee benefit plans other than pension plans.[2] 29 U.S.C. § 1003.

[2] The universe of employee benefit plans subject to ERISA comprises pension plans and welfare plans. 29 U.S.C. § 1002(3).

Pension plans include retirement income plans and deferred income plans. 29 U.S.C. § 1002(2)(A). Welfare plans include benefits for hospital and medical care, sickness and accident insurance, life insurance, disability payments, accidental death or dismemberment insurance, prepaid legal assistance, savings and vacation plans, scholarship funds, training programs and, as in this case, severance pay. 29 U.S.C. § 1002(1).

To ensure adequate supervision of employee benefit plans, employers are obligated to supply their workers with a clear and comprehensive description of every employee benefit plan. 29 U.S.C. § 1022. They also must file annual financial statements and other reports with the Department of Labor. 29 U.S.C. § 1023. To prevent the promise of retirement benefits from becoming illusory, workers must generally be considered eligible for pension plans within a year of starting their employment, 29 U.S.C. § 1052, and their accrued pension benefits must become increasingly nonforfeitable, or "vested," over time, 29 U.S.C. § 1053. Moreover, certain pension plans must satisfy minimum funding standards. 29 U.S.C. § 1082.

The Act also contains provisions directed against administrative mismanagement. These include the imposition of fiduciary responsibilities on plan administrators, 29 U.S.C. § 1104, and the creation of civil causes of action by which the Secretary of Labor or individual workers can enforce the administrator's fiduciary responsibilities, 29 U.S.C. § 1132. If a plan administrator breaches his fiduciary responsibilities, his potential liability is personal. He must compensate the plan for its resultant losses and disgorge to the plan any profits that he realized as a consequence of the breach. He is also subject to other appropriate relief, including removal from his position as plan administrator. 29 U.S.C. § 1109. Finally, to ensure that benefits will be paid even after the termination of a pension plan, as in the case of a plant closing, ERISA created the Pension Benefit Guaranty Corporation. 29 U.S.C. § 1302.

In enacting the safeguards of ERISA, Congress also recognized that excessive regulation of employee benefit

plans would be counterproductive. The legislative history of ERISA reflects congressional concern that high administrative costs would deplete the funds available for benefits,[3] and frustrate the "basic governmental policy of encouraging the growth and development" of private benefit plans.[4] Employers are not required to offer employees *any* benefit plans, and Congress believed that "if costs [were] made overly burdensome, particularly for employers," benefit plans would not develop as intended. 120 Cong Rec. H8702 (daily ed. Aug. 20, 1974) (statement of Rep. Ullman upon introducing the conference report). Thus, Congress imposed only minimum participation, vesting and funding standards on pension plans.[5] Moreover, Congress did not establish *any* participation, vesting or funding standards for welfare plans. 29 U.S.C. §§ 1051(1) and 1081(a)(1). Congress also permitted employers to maintain preferred methods of benefit plan administration. For example, when Congress was drafting ERISA, 60 percent of participants in private pension plans belonged to employer-administered plans. Staff of Senate Comm. on Labor and Public Welfare, 92d Cong., 2d Sess., *Statistical Analysis of Major Characteristics of Private Pension Plans* 31 (Comm. Print 1972). Congress facilitated this arrangement by allowing employers to appoint one of their officers or employees as the plan fiduciary. 29 U.S.C. §§ 1102(a)(2)

[3] 119 Cong. Rec. E6446 (daily ed. October 12, 1973) (statement of Rep. Nelsen).

[4] 120 Cong. Rec. H8702 (daily ed. August 20, 1974) (statement of Rep. Ullman upon introducing the conference report); 120 Cong. Rec. H1355 (daily ed. February 28, 1974) (statement of Rep. McKinney); 120 Cong. Rec. H8701 (daily ed. August 20, 1974) (statement of Rep. Dent).

[5] For example, employers need not include workers in their pension plans until they complete one year of service or reach the age of 21, whichever comes later. 29 U.S.C. § 1052(a)(1)(A). Moreover, the employer's contributions to an employee's retirement benefits need not become fully vested until the employee has completed at least ten years of service. 29 U.S.C. § 1053(a).

and 1108(c)(3). In all of these cases, Congress acted out of concern that the administrative cost of additional regulatory requirements would decrease the level of benefits or slow the rate of formation of new benefit plans. H.R. Rep. No. 807, 93d Cong., 2d Sess. 15 (1974).

In short, ERISA represents a careful and balanced effort to enact minimum and adequate employee safeguards that would not be unduly burdensome to employers and therefore "unfavorable rather than helpful to the employees for whose benefit [ERISA was] designed." 120 Cong. Rec. H8702 (daily ed. Aug. 20, 1974) (statement of Rep. Ullman upon introducing the conference report). See *Fort Halifax Packing Co.* v. *Coyne*, 107 S. Ct. 2211, 2217 (1987). Accordingly, the validity of the decision below must be evaluated against what Rep. Rostenkowski characterized as ERISA's "delicate" balance between stricter regulations for the protection of benefits and sufficient incentives to ensure the provision of benefit plans.[6]

The Decision Below

Respondents represent the class of non-union, salaried employees who were working in the Plastics Division of the Firestone Tire and Rubber Company and who continued in their jobs after the Division was sold in 1980 to the Occidental Chemical Corporation. Pet. App. A45. Before the sale, Firestone informed the employees in its Plastics Division that they would not be eligible for severance pay. Pet. App. A52. According to Firestone, its reduction in force provisions which governed severance pay did not apply when it sold an ongoing operation and its employees continued to work for the successor company with no significant loss in salary or benefits. Pet. App. A52.

Respondents brought this action in the United States District Court for the Eastern District of Pennsylvania

[6] 120 Cong. Rec. H8715 (daily ed. August 20, 1974) (statement of Rep. Rostenkowski).

under ERISA to recover severance pay and other benefits which they argued were due them as a result of the sale.[7] Despite their continued employment, respondents' theory was that the sale of the Plastics Division constituted "a reduction in force" by Firestone for which termination benefits were available under Firestone's Employee Handbook. Pet. App. A48. On cross motions for summary judgment, the district court found for Firestone on all of the respondents' then-pending claims. Pet. App. A73.

The court held that the determination that respondents were not entitled to reduction in force severance pay was neither arbitrary nor capricious. Pet. App. A56. The court noted that nothing in Firestone's policies or in the generally accepted meaning of the term "reduction in force" suggests that employees who remain in their jobs and continue to draw the same wages after the sale of a plant have suffered a termination because of a reduction in force. Pet. App. A53-A54.[8]

The court of appeals reversed. The Third Circuit recognized that "the clear weight of authority" among the courts of appeals supports use of the arbitrary and capricious standard to review decisions by administrators of benefit plans covered by ERISA. Pet. App. A8. Nonetheless, the court held that the denial of severance pay should be reviewed *de novo* in this case because Firestone faced a potential conflict of interest in deciding whether its assets should be used to satisfy respondents' claims for severance pay. Pet. App. A2-A3.

[7] Respondents also claimed retirement, stock and vacation benefits, which are described in the court of appeals' opinion. Pet. App. A4-A6. All of these claims have been withdrawn, settled or resolved in favor of Firestone. Pet. App. A3, A5-A6 n.2.

Certain individual respondents also sought damages under Section 502 (c) of ERISA, 29 U.S.C. § 1132 (c), for alleged deficiencies in Firestone's response to requests they made after the sale for information about Firestone's benefit plans.

[8] The court also denied respondents' Section 502(c) damages claims. Pet. App. A71-A72.

The court began its analysis by observing that the arbitrary and capricious standard was adopted for ERISA by analogy to cases concerning benefit plans governed by the Labor Management Relations Act ("LMRA") because the common law of trusts served as the basis of the fiduciary requirements imposed by Congress under both Acts. Pet. App. A14. The court noted, however, that the arbitrary and capricious standard could not be applied to ERISA without considering the differences between the LMRA and ERISA. Pet. App. A20-A21. Moreover, depending upon the method by which a benefit plan is funded, a denial of benefits by an administrator might mean that smaller contributions to the benefit plan would be required of the employer. Pet. App. A21-A22. The court stated that, in an employer-controlled, unfunded plan, the plan administrator faces a potential conflict of interest because his employer benefits when an employee's claim for benefits is denied. Pet. App. A24. Relying upon principles of trust law, the Third Circuit held that it should not defer to the judgment of the plan administrator in those circumstances. Pet. App. A24.

Having rejected the trust-based arbitrary and capricious standard of review for an employer-controlled, unfunded plan, the court of appeals turned to contract law for guidance and concluded that Firestone's adoption of a severance pay plan was an offer of a "unilateral contract" that its employees accepted by continuing employment with the company. Pet. App. A30. The court therefore held that the district court should not have deferred to the decision to deny benefits but should have determined for itself the validity of that decision "tak[ing] as [its] starting point the principles governing construction of contracts between parties bargaining at arms' length." Pet. App. A25.[9]

[9] The court also reversed the district court on the Section 502(c) damages claims. Pet. App. A39-A44. *Amici* take no position on this issue which is also before the Court.

SUMMARY OF ARGUMENT

In establishing ERISA's fiduciary requirements for administrators of employee benefit plans, Congress employed the language of trust law, thereby manifesting its clear intent to incorporate into ERISA judicial interpretations of that body of common law. *NLRB* v. *Amax Coal Co.*, 453 U.S. 322, 329-30 (1981). The legislative history of ERISA also demonstrates the intent of Congress to incorporate trust law principles into the fiduciary standards of ERISA. *Massachusetts Mutual Life Insurance Co.* v. *Russell*, 473 U.S. 134, 152 (1985) (Brennan, J., concurring). Consequently, this Court must turn to general principles of trust law in determining the standard of review under ERISA for decisions by benefit plan administrators. *Amax Coal*, 322 U.S. at 329-34.

Under the common law, courts ordinarily apply an abuse of discretion or arbitrary and capricious standard of review to decisions by trustees concerning the disposition of trust assets. 3 A. Scott & W. Fratcher, *The Law of Trusts* § 187.2 (4th ed. 1988). Based on this principle, all twelve of the federal circuits have adopted an arbitrary and capricious standard to review decisions by benefit plan administrators under ERISA, including the decisions of administrators who are employees of the companies which establish the plans.

The existence of a *potential* conflict of interest does not change the analysis. Under trust law, a potential conflict of interest for a trustee does not automatically require the court to review the fiduciary's decision *de novo*. *Flinchbaugh* v. *Chicago Pneumatic Tool Co.*, 531 F. Supp. 110, 114 (W.D. Pa. 1982). In particular, when the potential conflict was apparent at the time the trust was created by the settlor, the court will defer to the decision of the trustee unless there is *specific evidence* that there was an actual conflict of interest that was not apparent at the time the trust was created. See, *e.g.*, *Goldman* v. *Rubin*, 292 Md. 693, 441 A.2d 713, 724 (1982). When Congress passed ERISA, it recognized that plan administrators commonly would be employed by the

companies which established the plans and therefore would have a potential conflict of interest. Thus, the Third Circuit erred in applying the *de novo* standard solely on the basis of the administrator's potential conflict of interest and without any evidence that the administrator faced an actual conflict of interest.

The Third Circuit's decision would frustrate the goals of Congress when it passed ERISA. Congress expressly reserved to plan administrators the discretion involved in deciding claims for benefits. 29 U.S.C. §§ 1002(21)(A) and 1133(2). According to the court of appeals' reasoning, however, a substantial percentage of employee claims for benefits under ERISA would be subject to *de novo* review. Hence, the court's invocation of *de novo* review cannot be reconciled with the intent of Congress to leave decisionmaking primarily to plan administrators. Moreover, a *de novo* standard requires a time-consuming, fact-intensive judicial review. Consequently, the court of appeals' reasoning would impose substantial administrative burdens on pension plans that were not intended by Congress.

These burdens are not justified by any countervailing benefits. The fiduciary responsibilities of ERISA ensure that plan administrators will act solely in the interests of the employees. *Amax Coal*, 453 U.S. at 333-34. In addition, Congress chose to rely primarily upon actions by the Secretary of Labor or the employees for breach of fiduciary duty, instead of upon actions by employees to recover benefits allegedly due, for the enforcement of the fiduciary responsibilities. 120 Cong. Rec. S15742 (daily ed. Aug. 22, 1974) (statement of Sen. Williams upon introducing the conference report).

The arbitrary and capricious standard of review also ensures ample protection for employees. Courts have given the standard meaningful content and have closely scrutinized decisions by plan administrators when circumstances suggested that the decision was based on inappropriate grounds. *Holland* v. *Burlington Industries*, 772 F.2d 1140, 1149 (4th Cir. 1985), *cert. denied*, 477 U.S. 903 (1986). Hence, the Third Circuit's adoption of

a *de novo* standard is inconsistent with the congressional scheme and, in any event, unnecessary for the protection of employee benefits.

ARGUMENT

THE COURT OF APPEALS ERRED IN REFUSING TO APPLY THE ARBITRARY AND CAPRICIOUS STANDARD OF REVIEW TO A PLAN ADMINISTRATOR'S DECISION TO DENY RESPONDENTS' SEVERANCE PAY CLAIMS.

I. The Congressional Analogy Of Employee Benefit Plans To Common Law Trusts Indicates That Congress Intended To Adopt An Arbitrary And Capricious Standard Of Review.

A. The Statutory Language And Legislative History Indicate That Principles Of Trust Law Govern The Standard Of Review Of Decisions By ERISA Plan Administrators.

The terms of ERISA plainly describe the trust-like nature of the employee plans it regulates. Under ERISA, all such plans are described as "benefit" plans, 29 U.S.C. § 1002(3), and are administered by a "fiduciary," 29 U.S.C. § 1102. Individuals who may become entitled to benefits are characterized as "beneficiaries," 29 U.S.C. § 1002(8), and all assets of employee benefit plans are to be "held in trust." 29 U.S.C. § 1103(a). These are traditional trust terms. Restatement (Second) of Trusts §§ 2 and 3 (1959). Moreover, ERISA defines the nature of the fiduciary role in the same terms as trust law. Fiduciaries are granted "authority to control and manage the operation and administration" of benefit plans, 29 U.S.C. § 1102(a)(1), including the authority to decide claims, 29 U.S.C. § 1133(2). Compare Restatement (Second) of Trusts §§ 169 and 177. In addition, the administrator's authority and control are "discretionary." 29 U.S.C. § 1002(21)(A). Compare Restatement (Second) of Trusts § 187 comment a. Finally, the fiduciary of a benefit plan must

> discharge his duties . . . solely in the interest of the participants and beneficiaries . . . with the care, skill, prudence, and diligence . . . [of] a prudent man . . . [and] in accordance with the documents and instruments governing the plan . . . .

29 U.S.C. § 1104. Congress intended by using this language to track the classic description of a trustee's duties under the common law. See H.R. Rep. No. 533, 93d Cong., 1st Sess. 11 (1973); compare Restatement (Second) of Trusts §§ 170, 174 and 186.

When Congress enacted the language of trust law, it thereby expressed its intention to adopt generally accepted judicial interpretations of that language. *NLRB* v. *Amax Coal Co.*, 453 U.S. 322, 329-30 (1981). This inference concerning the intent of Congress is particularly strong here because, when Congress passed ERISA, its use of traditional trust law language in the Labor Management Relations Act of 1947 ("LMRA") had been construed by the courts. In the LMRA, Congress codified the trustee's common law duty of loyalty, 29 U.S.C. § 186(c)(5), and the courts had consistently held that general principles of trust law apply to LMRA benefit plans. See, *e.g.*, *Gomez* v. *Lewis*, 414 F.2d 1312, 1314 (3d Cir. 1969); *Roark* v. *Lewis*, 401 F.2d 425, 429 (D.C. Cir. 1968); *Miniard* v. *Lewis*, 387 F.2d 864, 865 n.5 (D.C. Cir. 1967), *cert. denied*, 393 U.S. 873 (1968). For this reason, this Court has concluded that Congress' incorporation of trust law in ERISA "essentially codified the strict fiduciary standards" of the LMRA. *Amax Coal*, 453 U.S. at 332.[10] In short, the language of ERISA makes clear, as this Court has held, that the common law of trusts defines the responsibilities of an ERISA plan administrator.

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[10] Congress expressly recognized ERISA's relationship to the LMRA in the discussion of ERISA's enforcement provisions. When Senator Williams introduced the conference report for ERISA, he observed that Congress intended that actions brought by employees to enforce their benefit rights be "regarded as arising under the laws of the United States, in similar fashion to those brought under . . . the Labor Management Relations Act." 120 Cong. Rec. S15742 (daily ed. Aug. 22, 1974). *See Grossmuller v. United Automobile Aerospace and Agricultural Implement Workers*, 715 F.2d 853, 857 (3d Cir. 1983).

Central States Pension Fund v. *Central Transp.*, 472 U.S. 559, 570-74 (1985); *Amax Coal*, 453 U.S. at 332.[11]

The legislative history also unambiguously demonstrates that Congress intended to incorporate trust law principles into ERISA. *Massachusetts Mutual Life Insurance Co.* v. *Russell*, 473 U.S. 134, 152 (1985) (Brennan, J., concurring). The committee reports and congressional statements are explicit that ERISA codified the fiduciary standards of trust law in the statute. H.R. Rep. No. 533, 93d Cong., 1st Sess. 11 (1973) ("[t]he fiduciary responsibility section, in essence, codifies and makes applicable to these fiduciaries certain principles developed in the evolution of the law of trusts"); H.R. Conf. Rep. No. 1280, 93d Cong., 2d Sess. 295 (1974) ("[t]he labor law provisions apply rules and remedies similar to those under traditional trust law to govern the conduct of fiduciaries"); 120 Cong. Rec. S15741 (daily ed. August 22, 1974) (statement of Sen. Williams upon introducing the conference report) ("[t]he objectives of [the fiduciary] provisions are to make applicable the law of trusts . . ."). The legislative history also demonstrates that Congress specifically intended the fiduciary standards of trust law to govern the ERISA claims-administration process. *Massachusetts Mutual*, 473 U.S. at 153 (Brennan, J., concurring).

In adopting the principles of trust law, Congress did not accept those principles in their entirety. H.R. Rep. No. 533, 93 Cong., 1st Sess. 11-13. Nevertheless, it plainly did not intend to alter the standard of judicial review of a fiduciary's decisions. There is no provision in ERISA modifying the standard of review nor was there any discussion in the legislative history about modifying the standard. This is significant because Congress

[11] Because the language of ERISA unambiguously reflects a decision by Congress to model the administration of employee benefit plans on that of common law trusts, further analysis of congressional intent is not necessary. *Jones* v. *MARTA*, 681 F.2d 1376, 1379 (11th Cir. 1982), *cert. denied*, 465 U.S. 1099 (1984).

specifically identified, and then modified, the principles of trust law which it felt were inconsistent with the purposes of ERISA. *Id.* at 12. Thus, for example, at common law, the creator of a trust may include an exculpatory clause in the trust agreement to shield the fiduciary from any liability for misuse of the trust's assets. *Id.*; Restatement (Second) of Trusts § 222. In enacting ERISA, Congress specifically precluded such exculpatory clauses. 29 U.S.C. § 1110. Similarly, under the common law of trusts, the creator of a trust may permit the trustee to make investments which would otherwise be prohibited as imprudent. H.R. Rep. No. 533, 93d Cong., 1st Sess. 12. In ERISA, Congress expressly condemned *all* imprudent investments. 29 U.S.C. § 1104.[12] In short, Congress' general approach was to adopt the common law of trusts. When it intended to make an exception, it did so.

The absence of any suggestion by Congress that it intended to modify trust law's standard of judicial review is particularly relevant in the context of pre-ERISA enforcement of entitlements to employee benefits. When it passed ERISA, Congress recognized that employees had generally relied upon "the traditional equitable remedies of the common law of trusts" to safeguard their benefits. S. Rep. No. 127, 93d Cong., 1st Sess. 5 (1973).[13] State courts applying trust law principles to disputes about employee benefits before ERISA had reviewed the plan administrator's decision under a deferential abuse of discretion standard. *Occidental Life Insurance Co.* v. *Blume*, 65 Wash.2d 643, 399 P.2d 76, 79 (1965); *Judge* v. *Kor-*

[12] Congress also stressed the duty of prudence. For example, fiduciaries must diversify investments to minimize the risk of large losses unless "it is clearly prudent not to do so." 29 U.S.C. § 1104 (a)(1)(C).

[13] Congress recognized that the inadequacy of pre-ERISA law lay not in the application of trust law remedies but in the absence of substantive requirements like vesting and funding. S. Rep. No. 127, 93d Cong., 1st Sess. 5 (1973). In other words, employees had remedies without rights.

tenhaus, 79 N.J. Super. 574, 192 A.2d 320, 328 (Super. Ct. 1963); *Whelan* v. *O'Rourke*, 5 A.D.2d 166, 170 N.Y.S.2d 284, 287 (1958); *Geron* v. *Kennedy*, 381 Pa. 97, 112 A.2d 181, 183 (1955). Thus, Congress must have assumed that this same deferential approach would be followed by federal courts in reviewing claims under ERISA.

Both the language and the legislative history of ERISA define the fiduciary responsibilities of benefit plan trustees in terms of common law trust principles. Consequently, this Court must turn to trust law to determine the standard of review under ERISA for decisions by benefit plan administrators. *Amax Coal*, 453 U.S. at 329-34.

B. Common Law Trust Principles Indicate That Courts Should Defer To The Decisions Of An ERISA Plan Administrator Despite His Potential Conflict Of Interest.

1. *Principles Of Trust Law Indicate That Courts Should Control A Plan Administrator's Exercise Of Discretion Only To Prevent Abuses Of That Discretion.*

The congressional choice of the trust model for ERISA is particularly relevant in this case with respect to the discretionary elements of benefit plan administration. According to trust law, the exercise of a trustee's powers is discretionary except when it is dictated by the terms of the trust or the principles of trust law. Restatement (Second) of Trusts § 187 comment a. Moreover, when the trustee exercises a discretionary power, courts cannot control that exercise "except to prevent an abuse by the trustee of his discretion." Restatement (Second) of Trusts § 187. Hence, courts have consistently declined to interfere with a trustee's discretionary decision unless the trustee abuses his discretion by acting arbitrarily, fraudulently, dishonestly or with an improper motive.[14]

[14] While courts employ several different verbal formulations for not deferring to a trustee's decision, these formulations are all tied to the reasonableness of that decision. Because the important point is that courts should defer to reasonable decisions by plan administrators, there is no need in this brief to focus on the differences among the alternative formulations which are, in any case, often not distinguishable. See *Citizens to Preserve Overton Park, Inc.* v. *Volpe*, 401 U.S. 402, 416 (1971) (defining arbitrary, capricious and abuse of discretion in the same way). Instead, for the sake of simplicity, it makes sense to subsume all of them under the rubric of "arbitrary and capricious."

3 A. Scott & W. Fratcher, *The Law of Trusts* § 187.2 (4th ed. 1988); *Jefferson National Bank* v. *Central National Bank*, 700 F.2d 1143, 1152 (7th Cir. 1983); *American Cancer Society* v. *Hammerstein*, 631 S.W.2d 858, 863 (Mo. 1981); *Gimbel* v. *Bernard F. and Alva B. Gimbel Foundation, Inc.*, 166 Conn. 21, 347 A.2d 81, 89 (1974); *Kuykendall* v. *Proctor*, 270 N.C. 510, 155 S.E.2d 293, 301-02 (1967); *Kloman* v. *Doctor's Hospital, Inc.*, 76 A.2d 782, 785 (D.C. 1950).

ERISA follows the approach of trust law in its treatment of the discretionary elements of benefit plan administration. To the extent that an individual is granted "discretionary authority or discretionary control respecting [the] management of [a benefit] plan," he assumes the role of a fiduciary. 29 U.S.C. § 1002(21)(A). As part of his administrative responsibilities, the fiduciary has the sole authority to decide whether a claim for benefits was properly denied. 29 U.S.C. § 1133(2). Accordingly, to the extent that a decision regarding a claim for benefits is discretionary, the discretion resides with the plan administrator.

Congress had considered and rejected the alternative approach of arbitration for resolving disputes over benefit claims. H.R. 2 in the Senate, 93d Cong., 2d Sess. § 691(a) (1974). Had arbitration been chosen, Congress would have deprived the fiduciary of discretion in deciding benefit claims. Hence, in rejecting arbitration, Congress further demonstrated its intent to vest the plan administrator with discretion in deciding benefit claims.

Because ERISA assigns the discretionary elements of the authority to decide claims to the plan administrator, it follows from trust law that courts can control the administrator in the exercise of his discretion only to prevent an abuse of discretion. Restatement (Second) of Trusts § 187. Consequently, all twelve of the federal circuits have applied the arbitrary and capricious standard of review to denials of benefits under ERISA.[15] The Third Circuit was simply incorrect when it suggested that these courts have "mechanically" applied the arbitrary and capricious standard from the LMRA to ERISA. As the previous discussion demonstrates, the arbitrary and capricious standard is derived directly from principles of trust law which Congress intended courts to follow in construing ERISA.[16]

2. *The Potential Conflict Of Interest Of An ERISA Plan Administrator Does Not Alter The Standard Of Review Because Congress Permitted The Potential Conflict.*

Under traditional trust law principles, the court below erred by declining to apply the arbitrary and capricious standard in the circumstances of this case. The court first observed that, because the Firestone plan administrator was Firestone itself and because denials of claims would redound to the benefit of Firestone, there was an inherent conflict of interest. Hence, the court concluded that "the principles of trust law require[d]" rejection of the arbitrary and capricious standard in favor of *de novo* construction of the trust document. Pet. App. A24. In effect, then, the court held that when a potential conflict of interest arises out of the structure of the benefit plan, *de novo* review is automatically required. This conclusion, however, is inconsistent with well-settled principles of trust law.

To be sure, courts will not and should not defer to trustees who act "from a motive other than to further the purposes of the trust." Restatement (Second) of Trusts § 187 comment g. However, the common law recognized the impracticality of eliminating all conflicts of interest. *Flinchbaugh* v. *Chicago Pneumatic Tool Co.*, 531 F. Supp. 110, 114 (W.D. Pa. 1982). Accordingly, "attenuated or hypothetical conflicts of interest" alone do not justify departure from the deferential standard. *Id.* See also *American Cancer Society*, 631 S.W.2d at 863-64; *Cosden* v. *Mercantile-Safe Deposit & Trust Co.*, 41 Md. App. 519, 398 A.2d 460, 471-72, *cert. denied*, 444 U.S. 941 (1979); *In re Thomas*, 311 A.2d 112, 114 (Del. 1973); *Burlingham* v. *Worcester*, 351 Mass. 198, 218 N.E.2d 123, 125-26 (1966); *Phelan* v. *Middle States Oil Corp.*, 220 F.2d 593, 604 (2d Cir.), *cert. denied*, 349 U.S. 929 (1955).

Moreover, trust law uniformly condones the existence of a *potential* or "hypothetical" conflict of interest if the potential conflict was readily apparent when the trust was created and was clearly accepted by the creator of the trust (the "settlor"). In such circumstances, courts do not decline to defer to a trustee because of the potential conflict unless it matured into an actual conflict.[17]

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[15] *Palino* v. *Casey*, 664 F.2d 854, 858 (1st Cir. 1981); *Schwartz* v. *Newsweek, Inc.*, 827 F.2d 879, 881 (2d Cir. 1987); *Northeast Dep't ILGWU Health and Welfare Fund* v. *Teamsters Local Union No. 229 Welfare Fund*, 764 F.2d 147, 162-63 (3d Cir. 1985); *Berry* v. *Ciba-Geigy Corp.*, 761 F.2d 1003, 1006 (4th Cir. 1985); *Bayles* v. *Central States, S.E. & S.W. Areas Pension Fund*, 602 F.2d 97, 99-100 (5th Cir. 1979); *Moore* v. *Reynolds Metals Co. Retirement Program for Salaried Employees*, 740 F.2d 454, 457 (6th Cir. 1984), *cert. denied*, 469 U.S. 1109 (1985); *Brown* v. *Retirement Committee of Briggs & Stratton*, 797 F.2d 521, 525-26 (7th Cir. 1986), *cert. denied*, 107 S. Ct. 1311 (1987); *Morgan* v. *Mullins*, 643 F.2d 1320, 1321 (8th Cir. 1981); *Jung* v. *FMC Corp.*, 755 F.2d 708, 711 (9th Cir. 1985); *Carter* v. *Central States S.E. and S.W. Areas Pension Plan*, 656 F.2d 575, 576 (10th Cir. 1981); *Helms* v. *Monsanto Co.*, 728 F.2d 1416, 1420 (11th Cir. 1984); *Maggard* v. *O'Connell*, 671 F.2d 568, 570-71 (D.C. Cir. 1982).

The Third Circuit, of course, has deviated from the arbitrary and capricious standard when a potential conflict of interest exists.

[16] The Third Circuit in its discussion of the standard of review, Pet. App. A7-A26, never cited the legislative history of ERISA.

[17] A potential conflict occurs when a trustee has a duty of loyalty only to the beneficiaries of the trust but has a relationship to a

G. G. Bogert and G. T. Bogert, *The Law of Trusts and Trustees* § 543(U), at 373 (rev. 2d ed. 1978); *Flinchbaugh*, 531 F. Supp. at 114; *Gregory* v. *Moose*, 266 Ark. 926, 590 S.W.2d 665, 670-71 (Ct. App. 1979) (Arkansas law); *State of Delaware* v. *Belin*, 456 So. 2d 1237, 1241 (Fla. Dist. Ct. App. 1984) (Florida law); *Lovett* v. *Peavy*, 253 Ga. 79, 316 S.E.2d 754, 756-57 (1984) (Georgia law); *Childs* v. *National Bank of Austin*, 658 F.2d 487, 490 (7th Cir. 1981) (Illinois law); *Fielder* v. *Howell*, 6 Kan. App. 2d 565, 631 P.2d 249, 251 (1981) (Kansas law); *Goldman* v. *Rubin*, 292 Md. 693, 441 A.2d 713, 714 (1982) (Maryland law); *Bank of Nevada* v. *Speirs*, 95 Nev. 870, 603 P.2d 1074, 1077 (1979), *cert. denied*, 449 U.S. 994 (1980) (Nevada law); *Renz* v. Beeman, 589 F.2d 735, 744-45 (2d Cir. 1978), *cert. denied*, 444 U.S. 834 (1979) (New York law); *Estate of McCredy*, 323 Pa. Super. 268, 470 A.2d 585, 600 (1983) (Pennsylvania law).[18]

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non-beneficiary that might cause him to breach that duty. *See, e.g., American Cancer Society*, 631 S.W.2d at 863. An actual conflict of interest occurs when the trustee has duties of loyalty to beneficiaries and non-beneficiaries that conflict with each other. *See, e.g., Childs* v. *National Bank of Austin*, 658 F.2d 487, 490 (1981). A potential conflict would mature into an actual conflict if the trustee allows his relationship to a non-beneficiary to actually influence his decisions.

[18] The Third Circuit did not rest its analysis on the basis that the challenged decisions arose in the context of a sale of a corporate division. Nevertheless, that fact does not alter the analysis. Under fundamental principles of trust law, the arbitrary and capricious standard applies when a fiduciary is acting to end the trust relationship. Restatement (Second) of Trusts § 334 comment d; G. G. Bogert & G. T. Bogert, *The Law of Trusts and Trustees* § 1000, at 314-17 (rev. 2d ed. 1983); 4 A. Scott, *The Law of Trusts* § 334.1, at 2644-45 (3d ed. 1967). Moreover, it also applies when the decision to end the trust relationship favors one beneficiary over the others and the trustee has ties to the favored beneficiary. *American Cancer Society*, 631 S.W.2d at 863. In such a setting, the court defers unless the claimant introduces specific evidence that there was an actual conflict of interest, rather than only a potential conflict. *Id.*

Thus, the judicial inquiry into a trustee's potential conflict is governed by the actual administration of the trust, not by the fact that the potential conflict of interest existed. *Belin* 456 So. 2d at 1240; *Lovett*, 316 S.E.2d at 757; *Goldman*, 441 A.2d at 723. Since potential conflicts that arise out of the structure of the trust fall into the category of those conflicts that are recognized in advance and accepted, trust law presumes that trustees are not influenced by structurally-based, potential conflicts.

The potential conflicts of interest that arise because the fiduciary of an employee benefit plan works for the employer were in fact recognized and accepted by Congress. When Congress passed ERISA, it knew that administrators of private pension plans commonly worked for the employer. According to a study of the private pension plan system undertaken by Congress, 60 percent of participants in private pension plans belonged to employer-administered plans. Staff of Senate Comm. on Labor and Public Welfare, 92d Cong., 2d Sess., *Statistical Analysis of Major Characteristics of Private Pension Plans* 31 (Comm. Print 1972). Nevertheless, Congress applied the same fiduciary standards to virtually all benefit plans,[19] without regard to who would administer them. 29 U.S.C. § 1101(a). Moreover, Congress expressly intended that agents of the employer, when serving as plan administrators, would exercise their discretion in administering ERISA plans despite their potential conflict of interest. 29 U.S.C. § 1108(c)(3) (permitting employers or their representatives to serve as fiduciaries); 29 U.S.C. § 1002(16)(A) (recognizing that the exercise of discretion is inherent in the role of a fiduciary). Analogizing Congress to the settlor in terms of the creation of the trust arrangement, it is plain that the relevant party envisioned the potential conflict of interest identified by the court of

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[19] The fiduciary standards do not apply to deferred compensation plans for select members of management or for highly compensated employees. 29 U.S.C. § 1101(a)(1). They also do not apply to payments to retired partners or the estates of deceased partners. 29 U.S.C. § 1101(a)(2).

appeals and condoned it. Under trust law, there is no basis for the court to ignore that decision and to scrutinize *de novo* all decisions arising out of that arrangement.

II. Adoption Of An Arbitrary And Capricious Standard Of Review Is Compelled By The Regulatory Scheme That Congress Enacted In ERISA.

A. A *De Novo* Standard Of Review Would Frustrate Congress' General Purposes In Passing ERISA.

A decision to retain the deferential standard of review, despite an apparent "conflict," would advance Congress' intent to grant employers "the freedom of decision-making vital" to the existence of employee benefit plans. S. Rep. No. 127, 93d Cong., 1st Sess. 13 (1973). Congress recognized that overly burdensome regulation of benefit plans would discourage employers from creating new plans or expanding existing plans. Moreover, higher administrative costs would also limit the growth and development of benefit plans. 120 Cong. Rec. H8702 (daily ed. Aug. 20, 1974) (statement of Rep. Ullman upon introducing the conference report). Hence, Congress established minimal standards under ERISA, reserving for employers considerable discretion to decide the substantive and administrative features of their benefit plans.

As discussed above, *supra* p. 16, Congress expressly assigned the discretion to decide benefit claims to the plan administrator. The Third Circuit's decision, however, would apply to the vast majority of benefit claims disputes thereby frustrating Congress' express intent to leave administration of these plans to the discretion of administrators. As the court of appeals itself explained, a potential conflict of interest arises out of the structure of a plan when (1) the benefit plan is administered by the employer and (2) the funding of the plan is such that a denial of benefits redounds to the advantage of the employer rather than another employee. For pension plans, this usually occurs for (1) single employer plans [20] that

[20] Pension plans are divided between single employer and multi-employer plans. While multi-employer plans are generally governed

are also (2) defined benefit plans.[21] A vast majority of pension plan assets are included in plans that meet these two criteria. According to 1981 data, of the nearly 700 billion dollars in private pension plan assets, 91 percent of the assets were held by single employer plans and 71 percent of the assets were held by defined benefit plans. Office of Pension & Welfare Benefit Programs, U.S. Department of Labor, *The Handbook of Pension Statistics 1985* 12 (1986).[22] For welfare plans, precise data are not readily available. Nevertheless, it is clear that the number of individuals involved here is also substantial. In the case of health care benefits, for example, a potential conflict would arise in the vast majority of plans.[23] Employers who self-insure directly profit from a denial of benefits. Moreover, employers who use third-party insurers gain from a denial since an employer's health insurance premiums are gen-

by employers and employees jointly, single employer plans are almost always administered by employers alone.

[21] Pension plans are divided between defined benefit and defined contribution plans. In defined benefit plans, the employer promises a specific level of benefits. For example, the monthly benefit might equal a sum of money times the number of years of employment. In defined contribution plans, the employer agrees to contribute a specified amount of money to the pension plan fund each year. When an employee is denied benefits from a defined benefit plan, the employer generally gains because a lower level of contributions will be needed to provide the promised benefits.

As this discussion indicates, the Third Circuit's apparent distinction between funded and unfunded plans does not adequately distinguish plans which may result in a potential conflict of interest from those that do not. Even with funded plans, there may be a potential conflict of interest.

[22] Preliminary data indicate that these percentages changed little between 1981 and 1984. Compare *The Handbook of Pension Statistics 1985*, *supra*, Table 1 at 18 with Pet. Amicus. Br. Table A at 1a. At the same time, total pension plan assets have doubled to almost 1.5 trillion dollars. *ERISA 1986 Report to Congress*, *supra*, at i.

[23] Over 20 million workers in medium and large firms receive health care benefits. Bureau of Labor Statistics, U.S. Department of Labor, *Employee Benefits in Medium and Large Firms, 1986* (Bulletin 2281).

erally based on the amount of benefits paid out in the previous year.

Given the high percentage of claims which would involve a "potential" conflict of interest as defined by the Third Circuit, it is impossible to reconcile the court's invocation of *de novo* review with Congress' intention to leave decisionmaking primarily to the plan administrators acting as fiduciaries. Congress did not intend for most claims to be decided by courts employing contract principles, and the court of appeals' failure to recognize this fact is fatal to the decision below.

A *de novo* standard of review would also contravene the intent of Congress to avoid burdensome regulation of employee benefit plans. With a *de novo* standard of review, there would be greatly increased incentives to litigate ERISA claims. That effect, together with the fact that judicial review would focus on the specific details of each claim, means that employee benefit plans would be subject to constant, time-consuming litigation. Continuously defending administrators' eligibility determinations would present administrative and financial strains on benefit plans. This case well illustrates the problem. The court of appeals has remanded respondents' claims for an analysis by the parties and the district court of the customary interpretation in the industry of this kind of severance pay provision, as applied to the sale of a business. Plainly, this inquiry will require substantial discovery by the litigants. In addition, the court of appeals has invited an inquiry into whether Firestone had done *anything* to give its employees reason to expect severance pay in the circumstances presented. Pet. App. A29-A31. This plainly opens up an enormous potential for discovery and a significant likelihood of a protracted hearing. Thus, the cost in terms of time, effort and money to the plan of proceeding further with this single class of claims may well prove to be enormous.

The administrative burdens in general would also be unjustifiably high. The coverage of ERISA is very broad. It protects the retirement income of approximately 42 million Americans who participate in nearly 800,000 private pension plans. *ERISA 1986 Report to Congress*, *supra*, at i. It also protects the benefits of the 65 million Americans who participate in the 4.5 million employer-sponsored welfare plans. *Id.* Hence, every time a worker submits a physician's or dentist's bill for reimbursement or every time a worker files for retirement benefits and the plan administrator denies the claim, in part or in full, a potential claim under ERISA arises that likely would be subject to *de novo* review.

B. The Arbitrary And Capricious Standard Fully Serves The Goals Of Congress.

1. *The Fiduciary Requirements Of ERISA Ensure That The Plan Administrator Serves The Interests Of The Plan Beneficiaries.*

Congress relied upon the arbitrary and capricious standard despite the widespread potential conflicts of interest because ERISA's fiduciary responsibilities ensure that plan administrators will act independently of the employers' interests. The court of appeals erred by implicitly assuming that, whenever a plan administrator is employed by the company whose plan is being interpreted, the administrator's interests will be identical to the company's.[24] However, the plan administrator's interests are defined by his functions, not his employment relationship. *Cf. Polk County* v. *Dodson*, 454 U.S. 312, 319 (1981). As this Court has observed, the fiduciary responsibilities of ERISA were designed to prevent the administrator from owing a duty of loyalty in his fiduciary role to anyone

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[24] This case is in a slightly unusual posture because respondents did not file any claims for severance pay with an administrator of the Firestone benefit plan. Nevertheless, the court of appeals analyzed the case under trust principles on the apparent assumption that the interpretation of the severance pay plan challenged by respondents was that of a fiduciary. Our analysis is based on the same assumption. If that assumption is not correct, the Court still should not permit the court of appeals' opinion to remain undisturbed as the law of the Circuit. Its use of an incorrect standard of review should be vacated and the matter remanded for an assessment of whether the posture of the case affects how the court of appeals would dispose of it.

other than the employees. *Amax Coal*, 453 U.S. at 333-34.[25] In particular, it is the administrator's duty to act *solely* in the interests of the benefit plan beneficiaries for the *exclusive* purposes of providing benefits to those entitled and defraying the reasonable costs of operating the plan. 29 U.S.C. § 1104(a)(1). Consequently, the effect of the fiduciary responsibilities is to ensure that a plan administrator does not represent the interests of any party, including those of the employer that appointed him, which would conflict with the interests of the employees. *Amax Coal*, 453 U.S. at 334.[26]

Congressional confidence that plan administrators would protect the interests of employees is illustrated by the legislative history. Congress expressly considered and rejected arbitration, 120 Cong. Rec. S15750 (daily ed. Aug. 22, 1974) (statement of Sen. Javits), and administrative review by the Department of Labor, 119 Cong. Rec.

[25] Moreover, the plan administrator has a relatively attenuated personal interest in the outcome of his decisions to grant or deny benefit claims. As a salaried employee of the company, his income does not directly or indirectly increase when fewer benefits are paid.

[26] Public defenders are not viewed as state actors even though the state fixes their compensation, hires their support staff, provides their office supplies and equipment, decides their case load—thereby effectively deciding the amount of time spent on each case—supervises their work and establishes general guidelines for them in carrying out their representation. *Polk County* v. *Dodson*, 454 U.S. at 331-333 (Blackmun, J., dissenting). Similarly, employees who act as plan administrators are not expected to act, nor do they act, as agents of their employers' interests when administering their employers' benefit plans.

Moreover, the employer's purposes in establishing a benefit plan are best served if the plan administrator acts solely in the interests of the beneficiaries. A plan administrator who acts otherwise compromises the harmony of employer-employee relations. This is true even if the beneficiaries are no longer employed by the company, as in the case of pension plans or severance pay plans. Current workers will not trust the promises to pay them benefits after they have left employment if the company fails to pay benefits to those who have already left employment.

S16899-900 (daily ed. Sept. 19, 1973) (statements of Sen. Hartke and Williams), as alternative approaches to the resolution of disputes over benefit claims. Thus, Congress concluded that plan administrators would be sufficiently independent decisionmakers such that review of their decisions should be deferential rather than *de novo*.

The effectiveness of ERISA's fiduciary responsibilities in maintaining the plan administrator's independence from the employer has been recognized by the Treasury Department as well. The Internal Revenue Code includes an exemption from the corporate income tax for certain employee benefit plans. 26 U.S.C. § 501(c)(9). In its implementing regulations, Treasury established as a criterion for tax exempt status that the benefit plan be an "employees'" plan. 26 C.F.R. § 1.501(c)(9)-1(a). This occurs when the plan is controlled by the membership of the plan or by independent trustees. 26 C.F.R. § 1.501(c)(9)-2(c)(3). A plan may satisfy the independent trustee requirement if it is an employee benefit plan subject to the fiduciary requirements of ERISA. 26 C.F.R. § 1.501(c)(9)-2(c)(3)(iii).

ERISA not only mandates fiduciary responsibilities; it subjects plan administrators to disciplinary action for violations of those responsibilities. Congress gave the Secretary of Labor primary responsibility for the enforcement of ERISA's fiduciary responsibilities. 120 Cong. Rec. S15742 (daily ed. Aug. 22, 1974) (statement of Sen. Williams upon introducing the conference report). In carrying out this responsibility, the Secretary may bring a civil action against a plan administrator for breach of his fiduciary duties. 29 U.S.C. § 1132(a)(2). If the court finds a breach of those duties, it will order the administrator to compensate the plan for any losses that resulted from the breach, 29 U.S.C. § 1109(a); *Massachusetts Mutual*, 473 U.S. at 140, and to turn over to the plan any profits realized by him in his use of the plan's assets, 29 U.S.C. § 1109(a). Moreover, the administrator may be removed from his position or be subject to any other remedies deemed appropriate by the court. *Id.* The

Secretary of Labor may also bring a civil action to enjoin any act or practice which violates the fiduciary responsibilities of ERISA or to obtain other appropriate equitable relief to either redress a violation of the fiduciary responsibilities or enforce these responsibilities. 29 U.S.C. § 1132(a)(5). Beneficiaries may bring the same causes of action as the Secretary of Labor to enforce ERISA's fiduciary responsibilities. 29 U.S.C. § 1132(a)(2) and (a)(5).[27] In view of the availability of this full range of remedies, it cannot lightly be assumed that Congress intended to turn routine claims to recover benefits into costly judicial searches for breaches of fiduciary duty.[28]

The procedural requirements of ERISA also provide good reason for the presumption that plan administrators employed by the company do not face an actual conflict of interest. First, these requirements directly limit the likelihood that a plan administrator will act on the basis of a potential conflict. Whenever a claim for benefits is denied, the benefit plan must set forth in writing the specific reasons for the denial, describe any additional material or information necessary for the employee to perfect the claim, and explain why that material or information is necessary. 29 U.S.C. § 1133(1); 29 C.F.R. § 2560.503-1(f). In addition, the plan must afford the claimant an opportunity for "full and fair review" of the decision denying the claim before the plan administrator. 29 U.S.C. §§ 1133(2) and 1102(a)(1).[29] These stringent

[27] An action to enforce ERISA's fiduciary requirements is distinct from an action to recover benefits. Compare 29 U.S.C. § 1132(a)(2) and (a)(5) with § 1132(a)(1)(B).

[28] Indeed, while Congress gave the federal courts exclusive jurisdiction over actions alleging a breach of fiduciary duty, it gave the federal and state courts concurrent jurisdiction over actions seeking the recovery of benefits. 29 U.S.C. § 1132(e)(1); H.R. Conf. Rep. No. 1280, 93d Cong., 2d Sess. 327 (1974).

[29] At a minimum, a plan administrator must inform the employee of what evidence he relied upon and provide the employee with an opportunity to review the evidence and present written comments

obligations to document the decisionmaking process make it very difficult for plan administrators to hide an arbitrary or capricious decision and therefore discourage them from acting out of improper motives. *Wolff v. McDonnell*, 418 U.S. 539, 565 (1974).[30] As a corollary, the documentation helps ensure that employees and courts will recognize when decisions are based on improper motives.[31] The employees or the Secretary of Labor will then be able to assert the rights of the employees in court and obtain relief. Finally, as a result of the procedural requirements, courts are presented with a record from which they can judge whether a reasonable decision was rendered without engaging in *de novo* review.

2. *The Arbitrary And Capricious Standard Provides Ample Protection For Employees.*

Congress relied upon the arbitrary and capricious standard also because it provides ample protection for employees. Under that standard, courts consider several factors, including whether the administrator has (a) construed the terms of the plan uniformly, (b) interpreted the plan in accordance with its terms, and (c) administered the plan in accordance with the requirements of ERISA. Comment, *The Arbitrary and Capricious Standard Under ERISA: Its Origins and Application*, 23 Duq. L. Rev. 1033, 1047-48 (1985); *Miles* v. *New York State Teamsters Conference Pension & Retirement Fund*

and/or documentary evidence in rebuttal. *Grossmuller*, 715 F.2d at 857-58 & n.5; 29 C.F.R. § 2560.503-1(g).

[30] Having to justify their decisions ensures that benefit plan administrators not only do not act unreasonably but also that they take the most appropriate action. In the process of explaining their decisions in writing, administrators must carefully analyze the bases of their decisions.

[31] If a denial of a claim for benefits is based on questionable logic, that will trigger suspicion and likely trigger an inquiry into the administrator's motives by the employee when the matter is before the district court.

Employee Pension Benefit Plan, 698 F.2d 593, 599 (2d Cir), *cert. denied*, 464 U.S. 829 (1983).[32]

Moreover, courts will take a "close look" at the administrator's determination whenever particular circumstances suggest that the administrator did not engage in "reasoned decisionmaking," *Maggard*, 671 F.2d at 571, or when the administrator acted fraudulently or in bad faith. *Sly* v. *P. R. Mallory & Co.*, 712 F.2d 1209, 1211 (7th Cir. 1983).[33] Thus, decisions by administrators based on inappropriate grounds can be, and have been, set aside under the arbitrary and capricious standard. *Van Boxel* v. *Journal Co. Employees' Pension Trust*, 836 F.2d 1048, 1052-53 (7th Cir. 1987); *Holland* v. *Burlington Industries*, 772 F.2d 1140, 1149 (4th Cir. 1985), *cert. denied*, 477 U.S. 903 (1986).[34]

[32] These factors naturally follow from the trust law principle that the exercise of a trustee's power is discretionary "except to the extent to which its exercise is required by the terms of the trust or by the principles of law applicable to the duties of trustees." Restatement (Second) of Trusts § 187 comment a.

[33] Although a "close look" involves greater care in examining the decision of the administrator, it nevertheless requires the court to approve the decision if it is based on the documents and instruments of the plan and it is not an unexplained deviation from prior decisions. Thus, even if the court itself would have decided the issue differently, it still must uphold the administrator's decision. Under a *de novo* standard, the court is not constrained at all by the administrator's interpretation of the plan or how that interpretation applies to the particular claim. Instead, the court decides whether the claim should be upheld based on contract principles. Under these principles, of course, the inquiry is much broader and therefore more burdensome on the parties. *See* p. 22, *infra*.

[34] The widespread use in federal law of the arbitrary and capricious standard demonstrates the confidence that Congress has in the standard's ability to protect individual interests. Decisions by federal administrative agencies are reviewed under that standard. 5 U.S.C. § 706. Congress also has adopted a standard of judicial deference for decisions by certain private parties. In particular, courts play "only a limited role" when reviewing the decisions of arbitrators. *United Paperworkers International Union* v. *Misco, Inc.*, 108 S. Ct. 364, 370 (1987). They "are not authorized to

While the arbitrary and capricious standard of review is appropriate for the vast majority of disputes involving employee benefit claims, traditional principles of trust law ensure that a *de novo* standard of review will be used as needed. Thus, for example, if the trustee has a direct and immediate financial stake in the outcome of a decision, the court will decide for itself which course of action is in the best interests of the beneficiaries. Restatement (Second) of Trusts § 187 comment g, illustration 2. Similarly, if an employee introduces evidence that the benefit plan administrator denied an employee's claim for benefits in order to realize a direct pecuniary gain, the court should subject the administrator's decision to *de novo* review.[35] No such showing was made or even attempted in this case.

* * * *

In sum, the Third Circuit's decision is inconsistent with the scheme established by Congress in ERISA. It ignores the important role Congress intended for plan administrators to play in making claims determinations. It discourages employers from creating or expanding benefit plans by imposing unduly heavy administrative burdens. Moreover, it substantially increases the expense of administering a benefit plan. What makes these burdens impossible to justify is that they will be imposed without adding significantly to the protection of employee benefits.

reconsider the merits of an award even though the parties may allege that the award rests on errors of fact or on misinterpretation of the contract." *Id.*

[35] For instance, an employee could make such a showing if the administrator's income were formally tied to the frequency of benefit denials. *Cf.*, *Tumey* v. *Ohio*, 273 U.S. 510 (1926); *NLRB* v. *Ohio New and Rebuilt Parts, Inc.*, 760 F.2d 1443, 1448 (6th Cir.), *cert. denied*, 474 U.S. 1020 (1985). Or, the employee might be able to show an informal tie, for example, if the administrator's yearly compensation tended to correlate with the financial performance of the benefit plan. In addition, a tie would exist if the employer had made clear, either explicitly or by his firings of previous plan administrators, that a plan administrator would not be kept on the job if too many benefits were paid out.

The Third Circuit obviously drew a different balance than did Congress when considering the costs and benefits of a *de novo* standard of review. But that is not the province of a court. As the Sixth Circuit observed, there is simply "no law" to support a stricter standard of review in ERISA cases. *Varhola* v. *Doe*, 820 F.2d 809, 813 (6th Cir. 1987). Congress struck a particular balance of interests when it selected trust law as the basis for implementing employee benefit plans. It was not for the court of appeals to substitute its judgment for Congress' concerning how these plans can best be administered. *Badaracco* v. *CIR*, 464 U.S. 386, 398 (1984). For this reason, the decision of the court of appeals should be set aside.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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June 9, 1988